ARIZONA WATER COMPANY

Docket No. W-1445A-02-0619

2002 RATE HEARING EXHIBIT NO. ___

For Test Year Ending 12/31/01

PREPARED

REBUTTAL TESTIMONY & EXHIBITS

OF

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BEFORE THE ARIZONA CORPORATION COMMISSION

IN THE MATTER OF THE APPLICATION OF ARIZONA WATER COMPANY, AN ARIZONA CORPORATION, FOR ADJUSTMENTS TO ITS RATES AND CHARGES FOR UTILITY SERVICE FURNISHED BY ITS EASTERN GROUP AND FOR CERTAIN RELATED APPROVALS.	Docket No. W-01445A-02-0619

REBUTTAL TESTIMONY OF SHERYL L. HUBBARD

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I. INTRODUCTION

Q. WHAT IS YOUR NAME, EMPLOYER AND OCCUPATION?

A. My name is Sheryl L. Hubbard. I am employed by Arizona Water Company (the "Company") as Manager of Rates and Regulatory Accounting.

Q. ARE YOU THE SAME SHERYL L. HUBBARD THAT PREVIOUSLY SUBMITTED DIRECT TESTIMONY IN THIS MATTER?

A. Yes, I am.

II. OVERVIEW, PURPOSE AND EXTENT OF TESTIMONY

Q. WHAT IS THE PURPOSE OF YOUR REBUTTAL TESTIMONY IN THIS PROCEEDING?

A. The purpose of my rebuttal testimony is to respond to certain direct testimony submitted by the Arizona Corporation Commission's Utilities Division Staff ("Staff") and the Residential Utility Consumer Office ("RUCO") in this rate proceeding. Specifically, I will present the Company's rebuttal position with respect to several elements of rate base including plant in service, accumulated depreciation, post test year plant additions, working capital allowance, deferred Central Arizona Project ("CAP") charges, and the Phoenix Office and Meter Shop allocations of plant-related items. In addition, I will address a number of items related to net operating income such as the revenue annualization, purchased power expenses, the Company's Purchased Power Adjustment Mechanism ("PPAM"), the Company's Purchased Water Adjustment Mechanism ("PWAM"), amortization of deferred CAP charges, water testing expenses, rate case expenses, and amortization of Contributions in Aid of Construction.

I also wish to note that, to the extent that Company witnesses rebut recommendations by Staff or RUCO regarding the Pinal Creek Group ("PCG") settlement that affect rebuttal schedules I have prepared for the Miami system, an explanation of those will also be incorporated into my testimony.

Q. SO YOUR TESTIMONY IN THIS PROCEEDING INCORPORATES RECOMMENDATIONS OF OTHER COMPANY WITNESSES?

A. Yes, it does. My testimony in this proceeding incorporates recommendations sponsored by the Company's President William M. Garfield, as well as by Vice-Presidents Ralph J. Kennedy and Michael J. Whitehead.

Q. ARE YOU SPONSORING ANY OF THE COMPANY'S REBUTTAL EXHIBITS AND SCHEDULES?

A. Yes, I am sponsoring the following exhibits, all of which are attached to this testimony:

Exhibit SLH-R1 Original Cost Rate Base-Net Plant
Exhibit SLH-R2 Original Cost Rate Base
Exhibit SLH-R3 Copy of letter from SRP dated 10/18/02
Exhibit SLH-R4 Analysis of PPAMs and PWAMs
Exhibit SLH-R5 Copy of Staff Policy on CAP Cost Recovery
Exhibit SLH-R6 Staff Response to AWC's Data Request No. 5.1
Exhibit SLH-R7 Staff Response to AWC's Data Request No. 6.1

Q. PLEASE SUMMARIZE THE COMPANY'S APPLICATION FOR RATE RELIEF IN THIS PROCEEDING.

A. The Company's application for a rate increase for its Eastern Group systems was filed on August 14, 2002. At the time the filing was prepared, the most recent calendar year for which audited financial statements were available was 2001. To make the actual 2001 test year ("TY2001") more representative of the period when new rates would be in effect for the Eastern Group, 2001 account balances and results of operations were annualized and normalized based on known and measurable changes. The Company's goal was then and remains now, the presentation of a level of operating income that reflects the operating results that will be realized when new rates authorized in this proceeding go into effect. In connection therewith, the Company included in adjusted test year plant an appropriate amount of its plant investment dedicated to the adjusted test year customers as needed to ensure that a fair value determination can be computed and fair and reasonable rates could be developed.

Q. WHEN ARE THE NEW RATES AUTHORIZED IN THIS PROCEEDING ANTICIPATED TO GO INTO EFFECT?

A. Currently we anticipate a Commission decision by the end of January 2004 meaning new rates should go into effect for February of 2004.

III. <u>USE OF UNADJUSTED HISTORICAL YEAR</u>

Q. IS IT SOUND RATEMAKING TO USE AN UNADJUSTED HISTORICAL TEST YEAR TO DETERMINE FUTURE RATES?

A. No, it is not. Determination of the test year may be the most significant single factor in the ratemaking process. The test period must be representative of the period when the rates will be charged and an assessment of how the period to be used compares to the period when the rates will be charged is mandatory. Unless an historical period's results of operation are adjusted to recognize changing conditions, the rates so determined cannot be fair and reasonable. Even in stable economic times, historic data typically requires restatement for actual occurrences not expected to reoccur or for events that are expected to occur but did not exist (in whole or in part) in the historical unadjusted test year.

These adjustments, normalizing to restate an historical period for abnormal conditions, annualizing to reflect an annual level of revenue or expense for items included for a partial year that should be either increased or eliminated, out-of-period adjustments to adjust for items not properly reflected in the period, reclassification of items to add or remove items for purposes of rate recovery and adjusting for known and measurable changes in events or conditions that will affect future cost or revenue levels, must be considered and taken into account. Absent such adjustments, the rates determined will be distorted, either too low or too high, and will not be fair or reasonable.

Q. DOESN'T RUCO RECOMMEND THAT THE COMMISSION SET RATES BASED ON AN UNADJUSTED HISTORICAL TEST PERIOD?

A. Strictly speaking, RUCO clearly wishes to have the Commission set rates for the Eastern Group based on an unadjusted test year. *See, generally,* Direct testimony of William A. Rigsby and Direct testimony of Timothy J. Coley. However, having unsuccessfully advanced this same position in other ratemaking proceedings, including the Company's recent Northern Group rate case, RUCO now seeks, in essence, to change the test year used in this proceeding from a 2001 adjusted test year to an unadjusted 2002 test year.

Q. WHAT IS WRONG WITH RUCO'S POSITION?

A. To begin with trying to use 2002 as the test year in this proceeding violates the definition of test year in R14-2-103A.p. Moreover, it is inappropriate to use operating results that have not been analyzed to determine if 2002 is a representative period for basing future rates. This problem is exacerbated by the limited time allowed for the Company to prepare rebuttal testimony in this proceeding, a time frame in which it is impossible for Arizona Water to alter the test year and then determine specific deficiencies that exist in using an unadjusted 2002 historical period. Therefore, we urge the Commission to again reject RUCO's position and to utilize an adjusted 2001 test year to determine the Eastern Group's rates in this proceeding.

IV. RATE BASE

A. Plant In Service

Q. DOES THE COMPANY AGREE WITH STAFF'S PROPOSED PLANT IN SERVICE FOR THE SYSTEMS IN THE EASTERN GROUP?

A. No, although Staff and the Company do not appear to be far apart. Staff's calculations of Plant in Service for each system in the Eastern Group reflect Staff's erroneous removal of all of the actual, test year plant in service balances associated with the Phoenix Office and Meter Shop plant. The effect of this removal is an understatement in the Eastern Group's Rate Base of $1,615,233. Exhibit SLH-R1 sets forth the appropriate adjusted test year balances for the Eastern Group's Gross Plant in Service. Line 1, Gross Plant in Service, column (d) Rebuttal Adjusted TY, shows the Company's rebuttal calculation of Gross Plant In Service, which includes actual revenue neutral post-test year plant additions, to be $82,717,891. The Phoenix Office Allocation and Meter Shop Allocation, including the applicable revenue-neutral post-test year plant additions should be $1,758,733 and $38,139, as shown on lines 2 and 3 column (d), respectively. Thus, the total Gross Plant in Service for the Eastern Group should be $84,514,764. Stated simply, if Staff's recommended Gross Plant In Service for the Eastern Group of $82,899,530 is adjusted for the exclusion of the Phoenix Office and Meter Shop test year plant of $1,615,233, Staff-revised Plant in Service is $84,514,764, which the Company would accept as an appropriate amount for Gross Plant in Service. Exhibit SLH-R1 consists of nine pages setting forth the net plant recommendation for each of the individual Eastern Group systems.

B. Accumulated Depreciation

Q. STAFF IS RECOMMENDING AN ADJUSTMENT TO THE ACCUMULATED DEPRECIATION BALANCE TO REFLECT AN ADDITIONAL FULL-YEAR DEPRECIATION ON THE ADJUSTED TEST YEAR PLANT IN SERVICE. DOES THE COMPANY AGREE WITH THIS METHODOLOGY?

A. No, and the Staff provides no rationale for increasing the accumulated depreciation balance. *See* Direct Testimony of Ronald E. Ludders ("Ludders Direct") at 21. Staff ignores the adoption in this proceeding of a 2001 test year showing a deterioration in earnings, the very circumstances that prompted the filing of a rate application. The Company's pro forma adjustment to plant in service for the non-revenue producing post-test year plant is merely an attempt to partially reduce the effects of regulatory lag in obtaining rate relief to allow the Company an opportunity to earn a fair rate of return on investments to serve test year end customers. It is the Company's intention that the post-test year plant additions be treated as if (pro forma) the investment were in service at the end of the test year. Therefore, accumulated depreciation should not be adjusted for any more than the additional depreciation expense that will be computed on the year-end balance including the pro forma post-test year plant additions.

In contrast, if an additional year of depreciation is computed and used to reduce the Company's rate base, the Company's opportunity to earn a fair rate of return on its recognized investments is further hindered. While the Company is awaiting a final decision, the deterioration in earnings continues.

Q. BUT ISN'T THE COMPANY RECOMMENDING A PRO FORMA ADJUSTMENT TO DEPRECIATION EXPENSE?

A. Yes, but this is different than Staff's (and RUCO's) recommended adjustments to accumulated depreciation. The purpose of the Company's pro forma adjustment to depreciation expense is to recognize the known and measurable change in test year 2001 operating cost levels that will result from additional depreciation on plant not previously included in the depreciation calculation or in the Company's rates.

Jurisdictions that recognize an additional adjustment to the accumulated depreciation balance concurrently include an equal amount of depreciation expense in the calculation of operating expenses. In other words, the pro forma adjustment to annualize the depreciation expense may also be used to increase the accumulated depreciation balance in the rate base calculation. The Company's calculations conform to this conventional treatment. The pro forma depreciation expense adjustments and the adjustment to the accumulated depreciation are, in fact, identical.

Staff's pro forma depreciation expense and associated adjustment to the accumulated depreciation are not. To illustrate, the Staff's pro forma depreciation expense adjustment for Apache Junction is a reduction of $212,006 while the adjustment to accumulated depreciation for Apache Junction is an increase of $1,210,940 ($1,307,339-$96,399). The appropriate accumulated depreciation balance of $18,157,533, which recognizes the Staff's recommended levels of post-test year plant additions is shown at line 5, column (d) on Exhibit SLH-R1.

Q. ARE THERE OTHER DEFICIENCIES IN STAFF'S PROPOSED ADJUSTMENTS TO THE ACCUMULATED DEPRECIATION BALANCE?

A. Yes. Upon closer examination of the supporting working papers provided by Staff, Staff's calculation of the accumulated depreciation balance of $19,835,625 (total Eastern Group) has <u>not</u> been adjusted for the reduction in depreciation expense that occurs when plant is retired. This adjustment is necessary to properly reflect the half-year convention that the Company uses to depreciate plant additions in the year the plant is placed in service. The same half-year convention applies in the year that the property is retired. Staff's calculations encompass the period from the last Arizona Water Company rate decision for the Eastern Group in 1991 through December 31, 2002. As such, the adjustment is overstated by the effect of the half-year conventions on all retirements of plant over a twelve-year period.

Q. HAVE YOU PREPARED A SCHEDULE COMPARING THE STAFF'S RECOMMENDED ACCUMULATED DEPRECIATION TO THE COMPANY'S?

A. Yes. Exhibit SLH-R1 is a summary of Net Plant as set forth in the Company's application compared to Staff's recommendation for Net Plant. This schedule shows the Company's revised or, more accurately, rebuttal position for accumulated depreciation to recognize the affects of the changes in post-test year plant additions that the Company is adopting in its rebuttal presentation. The Staff's proposed level of Accumulated Depreciation of $19,835,625 contains several errors as discussed above, and should not be relied upon. As such, the Company is recommending an Accumulated Depreciation balance for the adjusted test year of $18,157,533 as shown on Exhibit SLH-R1, line 5, column (d).

Q. WHAT AMOUNT OF NET PLANT IS THE COMPANY RECOMMENDING IN ITS REBUTTAL FILING?

A. The Company is recommending Net Plant for its Eastern Group systems of $66,357,231 as shown on Exhibit SLH-R1, line 8, column (d).

C. Post Test Year Plant Additions

Q. HAS THE COMPANY REVIEWED THE STAFF'S RECOMMENDATIONS CONCERNING POST TEST YEAR PLANT ADDITIONS?

A. Yes. Mr. Whitehead explains the Company's response to the Staff's recommended Post Test Year Plant Additions. *See* Exhibit MJW-R1, attached to the Rebuttal

Testimony of Michael J. Whitehead.

D. Working Capital Allowance

Q. DO YOU AGREE WITH STAFF'S USE OF A 592 LAG DAY FACTOR IN CALCULATING THE CASH WORKING CAPITAL COMPONENT RELATED TO PROPERTY TAXES?

A. No, we do not. The lead/lag method of computing the cash working capital component of rate base requires a calculation of the lead days (prepayments) or lag days (accruals) that exist between the time an expense is recorded and the payment of such expenses. Although it is generally accepted that property taxes have a payment lag, Staff has exaggerated the actual lag 2.8 times. While the Department of Revenue recently modified the methodology for determining property taxes for water utilities in Arizona; it did not revise the billing or payment requirements, including the timing of the payments. The property taxes that the Company accrues in January through June of any given year are payable in November of that same year, while the property taxes that are accrued in July through December are payable in May of the following year.

It follows that the extended lag should be an average of 212 days versus Staff's 592 lag days. 212 lag days represents the same number of lag days adopted by this Commission for property taxes in the Company's Northern Group case utilizing a 1999 test year. Decision No. 64282 (December 28, 2001). RUCO witnesses have also computed the lag days for property taxes at 212 days. *See, e.g.*, Schedule WAR-7 page 2 of 4. I would also note that this is the same number of lag days that APS used in its recently filed rate application. *See* Testimony of Laura L. Rockenberger (Docket No. E-01345A-00437) at attachment LLR-3. Staff has clearly computed the property tax lag incorrectly for working capital purposes. Adopting the Company's lag day calculation for working capital purposes results in an adjustment of $1,264,932 to the Staff's working capital allowance of ($1,054,873) on a total Eastern Group basis.

Q. HAS THE COMPANY IDENTIFIED OTHER CONCERNS WITH THE CALCULATION OF THE CASH WORKING CAPITAL ALLOWANCE PROPOSED BY STAFF?

A. Yes. In his direct testimony, Mr. Ludders discusses five adjustments to the Company's analysis that resulted from Staff's analysis of the Company's lead-lag analysis. Ludders Direct at 9, ls. 11-18. Of the five adjustments identified, only two adjustments are consistent with the working papers provided in support of the Staff's working capital calculation: item (3) "Staff recognized interest expense" and (5) "Staff used a method that eliminates the mismatch between the dollar amount included in the dollar-day revenue and dollar-day expense lag amounts by comparing revenue lag days directly to payment lag days"..

The other three identified adjustments to the Company's analysis are not consistent with the working papers Staff provided. More specifically, (1) "Staff used expense amounts and expense lag days for each individual system" implies that the Company's working capital calculation did not use an individual system approach; (2) "Staff removed depreciation expense and deferred income taxes from the calculation of expense lag days" implies that the Company's calculation of expense lag days included depreciation expense and deferred income taxes; and (4) "Staff incorporated its adjustments to operating expenses." In each instance Staff's inferences are in error.

Schedule B-6, page 3 of 3 of the Company's 2002 Rate Hearing Exhibit specifically has the notation "N/A" (denoting not applicable) in the column labeled Average (Lead)Lag Days calculating the expense lag days for depreciation expense and deferred income taxes. In reference to operating expenses, Staff did not incorporate its adjustments to operating expenses as stated in their witness' direct testimony. The operating expenses used by Staff are the same as are included in the Company's working capital calculation. Thus, Staff's calculation of the working capital allowance is unreliable and cannot form the basis for determining an appropriate working capital allowance in this proceeding.

Q. STAFF HAS ADJUSTED THE COMPANY'S WORKING CAPITAL ALLOWANCE TO REFLECT A LAG ASSOCIATED WITH THE PAYMENT OF INTEREST. IF STAFF'S RECOMMENDATION IS ADOPTED, WHAT IS THE EFFECT ON THE COMPANY'S REBUTTAL PRESENTATION?

A. Using the Company's Rate Base presented on Exhibit SLH-R2, the interest payment lag would be calculated by computing the applicable system's interest expense (rate base times the weighted cost of debt) and applying the Staff's lag days factor of .25 (91.25 lag days divided by 365 days) to compute the necessary reduction in the Company's working capital allowance. On an Eastern Group basis, the reduction in the Company's requested working capital allowance is approximately $255,000.

E. Deferred Central Arizona Project Charges

Q. HAS THE COMPANY REVIEWED THE STAFF'S PROPOSED TREATMENT OF DEFERRED CENTRAL ARIZONA PROJECT COSTS?

A. Yes. Staff is recommending continued inclusion in rate base of the unamortized balance of the $60,000 deferred CAP charges authorized in Decision No. 58120 (December 23, 1992) and the net balance of the Company's actual deferred Cap M&I charges incurred from 1993 through December 31, 2002. Although Staff used the Company's original deferred CAP balance of $704,903 in the calculation of its recommended revenue requirement, the actual 2002 balance as discussed in

Staff' testimony is $691,522 ($46,315 + $645,207).

Q. WHAT AMORTIZATION PERIOD IS THE STAFF RECOMMENDING FOR RECOVERY OF THE DEFERRED CAP M&I CHARGES?

A. Frankly, it is unclear, even though we have reviewed Staff's direct filing, whether Staff is proposing to amortize the deferred CAP M&I charges over a period of 32 or 34 years.

Q. DOES THE COMPANY AGREE WITH A 32 OR 34-YEAR AMORTIZATION PERIOD FOR RECOVERY OF THE DEFERRED CAP M&I CHARGES?

A. Absolutely not. The basis of Staff's recommendation is that the deferred CAP M&I charges are an asset with some future benefit. This is just not the case. The M&I charges are a lease payment, if you will, for the use of the Central Arizona Project canal system for the annual delivery of up to 6,000 AF of Colorado River water for the Apache Junction system for the period of the CAP contract. The M&I charges were deferred by Arizona Water until such time as its CAP allocation was being fully utilized. Arizona Water has been using a portion of its annual allocation for potable consumption since prior to entry of Decision 58120 without cost recovery of the CAP M&I charges.

Q. HAS THE COMMISSION ADDRESSED THE RECOVERY OF DEFERRED CAP M&I CHARGES ?

A. Yes. As I discussed in my direct testimony (at 13-15), Commission Decision No. 62993 (November 3, 2000) directed Staff to develop a policy statement regarding recovery of costs related to CAP. In that policy statement, the Staff identified criteria required to demonstrate compliance and obtain CAP cost recovery. The policy statement is attached as Exhibit SLH-R5.

Q. IS ARIZONA WATER COMPANY ABLE TO DEMONSTRATE

COMPLIANCE WITH THESE IDENTIFIED CRITERIA?

A. Yes. Again, as shown in my direct testimony (at 13-15), Arizona Water has demonstrated compliance with each of the criteria identified in the Staff's policy statement regarding recovery of CAP costs.

Q. HAS THIS COMMISSION ADDRESSED THE RECOVERY OF DEFERRED CAP M&I CHARGES FOR OTHER WATER UTILITIES?

A. Yes. In Decision No. 62293 (February 1, 2000), the Commission addressed the recovery of deferred CAP M&I charges for Sun City Water Company and Sun City West Utilities Company, now operational districts of Arizona-American Water Company. In that case, following a determination that the CAP water was "used and useful", the deferred CAP charges were amortized over the period that the charges had accumulated, a period of five years, which resulted in a 60-month amortization period.

Q. FOLLOWING THE SAME APPROACH, WHAT WOULD BE THE APPROPRIATE AMORTIZATION PERIOD FOR ARIZONA WATER?

A. In 1993, Arizona Water began deferring the CAP M&I charges that comprise the $645,207 balance at December 31, 2002. The test year in this case has been adjusted for the known and measurable deferred CAP M&I charges through December 31, 2002. Following the Commission's reasoning in Decision No. 62293, the amortization period should be no longer than the period over which the M&I charges were billed, which in the Company's case would be nine years.

Q. IS THE COMPANY MODIFYING ITS REQUEST TO AMORTIZE THE DEFERRED CAP M&I CHARGES FROM ITS ORIGINAL REQUEST FOR A THREE-YEAR AMORTIZATION?

A. No. The Company set forth its rationale for requesting a three-year amortization in its direct testimony (*See* Hubbard Direct at 28) and is not convinced that other amortization periods are more reasonable given Arizona Water's individual circumstances.

Q. WHAT ABOUT RUCO'S RECOMMENDATIONS REGARDING THE AMORTIZATION PERIOD FOR DEFERRED CAP M&I CHARGES?

A. RUCO, consistent with its use of an unadjusted 2002 historical test year, is recommending the amortization of the deferred CAP M&I charges balance at December 31, 2002 over a period not less than ten years. Although the recommended ten-year amortization period is reasonable, the amount that RUCO recommends be amortized is entirely unsupported by the evidence. RUCO recommends that the Company be limited to the $645,207 deferred as of December 31, 2002, which permanently eliminates the recovery of the CAP M&I charges deferred in 2003 and the period in 2004 prior to the time the new rates become effective. Thus, RUCO's position is punitive and confiscatory. The charges are a legitimate cost of providing water to Arizona Water's customers and as such should not be disallowed.

F. Phoenix Office And Meter Shop Allocations Of Plant-Related Items

Q. PLEASE DISCUSS THE STAFF'S TREATMENT OF PHOENIX OFFICE AND METER SHOP ALLOCATIONS OF PLANT-RELATED ITEM.

A. In general, the Staff's presentation begins with the Company's filed positions. Recommended levels of rate base elements such as plant, accumulated depreciation, and working capital were determined and the Company's requested amounts were adjusted to the Staff recommended level. In the Company's presentation, test year rate base for the Phoenix Office and Meter Shop were computed and subsequently allocated to the individual systems as two separate line items labeled Phoenix Office Allocation and Meter Shop Allocation set forth on the Company's Schedule B-1.

The Post Test Year Plant Additions associated with the Phoenix Office and Meter Shop allocations, on the other hand, were included with the Post Test Year Plant Additions Pro Forma adjustment of each individual system presented on the Company's Schedule B-2. When the Staff computed its recommended Post Test Year Plant Additions associated with the Phoenix Office and the Meter Shop, it, apparently inadvertently, adjusted the test year level of plant for the Phoenix Office Allocation and the Meter Shop Allocation, effectively eliminating the test year plant in service for the Eastern Group allocation of the Phoenix Office and Meter Shop plant. The effect of this error is an understatement of plant in service of $1,615,234 as discussed above (at 5).

G. PCG Settlement-Rate Base Effects

Q. DOES THE COMPANY PROPOSE ANY ADJUSTMENTS TO REBUT STAFF'S RECOMMENDED TREATMENT OF THE PCG SETTLEMENT?

A. The Staff is recommending a net reduction in the Miami system's rate base of $1,350,000. This includes a rate base reduction of $1,400,000 with a corresponding deduction of accumulated amortization of $50,000 as shown on Miami Staff Exhibit REL-7. To adopt and incorporate the Company's rebuttal position, as explained more thoroughly in the rebuttal testimonies of Mr. Garfield and Mr. Kennedy, a reversal of Staff's adjustment to rate base is necessary. The effect of this reversal will be to restore $1,400,000 to the rate base of the Miami water system. Adopting the Company's rebuttal recommendation will also result in an adjustment to Net Operating Income to reverse the effect of the amortization expense adjustment, which is explained below.

Q. TO INCORPORATE ALL OF THE FOREGOING RATE BASE-RELATED ADJUSTMENTS, HAVE YOU PREPARED AN EXHIBIT OF THE

COMPANY'S REQUESTED RATE BASE IN ITS REBUTTAL PRESENTATION?

A. Yes, Exhibit SLH-R2 is a nine-page schedule that summarizes the Company's Original Cost Rate Base in this rebuttal presentation for each of the Eastern Group systems. The Eastern Group Original Cost Rate Base requested is $39,002,876.

V. NET OPERATING INCOME

A. Revenue Annualization

Q. DOES THE COMPANY AGREE WITH THE STAFF'S RECOMMENDED ADJUSTMENT TO THE COMPANY'S REVENUE ANNUALIZATION PRO FORMA ADJUSTMENT?

A. The Company has reviewed the basis of the Staff's recommended change in the Revenue Annualization Pro Forma adjustment and is of the opinion that the Company's adjustment as originally calculated more accurately represents the increase in revenues necessary to adjust the test year operating results to a year end level of customers. The Company computed average revenue per customer using only the 5/8-inch meter size because the majority of the growth in the Eastern Group systems for the test year occurred in the 5/8-inch meter group, as shown on the following table.

Customer Class	Increase in # of Customers	% of Total
Residential	588	98%
Commercial	7	1%
Industrial	1	.2%
Fire Sprinkler	7	1%
Other	-2	-.3%
Total	601	100%

By computing and applying an average revenue per customer using all customer classes to the test year end increase in customers, as Staff is proposing, the revenue annualization is overstated because increases that will not occur are reflected in the proposed adjustment. Staff has applied to 588 customers $160 of additional revenue which will not materialize, an overstatement in revenues for the Eastern Group of no less than $94,080 (588 X ($510-350)).

B. Purchased Power Adjustment Clause

Q. DOES THE COMPANY AGREE WITH STAFF'S RECOMMENDED ELIMINATION OF THE COMPANY'S PURCHASED POWER ADJUSTMENT MECHANISM?

A. No, we do not agree. There are several reasons to continue the purchased power adjustment mechanism ("PPAM") for Arizona Water Company at this time. For one thing, the Company purchases electricity to pump water from several electric providers, including, among others, Arizona Public Service Company ("APS"), Salt River Project ("SRP"), and Navopache Electric Cooperative ("NEC"). SRP and NEC have adjustor mechanisms for their power costs that allow them to unilaterally adjust the charge to Arizona Water for electric power. See Exhibit SLH-R3.

If viewed in isolation, i.e., on an individual system basis, the PPAM factors approved in the Company's latest PPAM filing may seem insignificant. However, the effect is more significant over longer time periods and on a total Company basis, as shown on Exhibit SLH-R4. Although Staff complains about the level of work required, without any real explanation of the alleged burden, the truth is, the Company minimizes the number of filings by aggregating all systems affected by a utility's power change in a single application, thus performing the majority of the work necessary to document the requested changes for Staff to review as part of the

PPAM filing. Staff seeks to trivialize the PPAMs approved in 2003 by reflecting the net change requested. *See* Ludders Direct at 10. What is more important to note is the fact that PPAMs are currently providing <u>reduced</u> purchased power costs to customers of approximately $63,000 annually in the Eastern Group, and $198,000 annually on a company-wide basis. Without the PPAMs, these reductions would not have been passed on to the Company's customers except following the establishment of new rates in a rate case.

Moreover, a PPAM provides benefits for both the customer and the Company. Since 1996, under the terms of several settlement agreements, APS has been reducing its rates annually. Through the PPAM, Arizona Water has been able to pass those reductions to its customers. In addition, it is the Company's understanding that APS is currently before the Commission seeking to implement a PPAM in its rates and charges to allow it to better reflect the market price of power in its retail rates. And, we further understand APS recently filed a request for a rate increase with the Commission. Without a PPAM, both customers and the Company will be unable to reflect rate changes whether the change is an increase or a decrease, absent filing a complete rate case filing. This is neither fair to the Company or ratepayers and makes little sense from a standpoint of administrative and regulatory efficiency.

In summary, therefore, with the electric power industry still in a transitional stage, power costs, one of the Company's most substantial operating costs will not remain at their current levels clearly making it the wrong time to eliminate the PPAM.

Q. BUT ISN'T IT STAFF'S POSITION THAT ARIZONA WATER COMPANY IS THE ONLY WATER PROVIDER STILL USING THIS ADJUSTOR?

A. That is not a persuasive reason at all. Per Staff's Response to the Company's Data

Request No. 6.2, copy attached as Exhibit SLH-R7, Bella Vista Water is the only water provider other than Arizona Water that had a PPAM in the last ten years. Bella Vista's PPAM was eliminated in 1999 but it was eliminated pursuant to a settlement agreement, and not without reservations. The more relevant language from the settlement is:

> The elimination of the PPAM in this proceeding shall not be used by the Arizona Corporation Commission Staff, the Arizona Corporation Commission or RUCO to support the denial of the PPAM in the future. (Exhibit A to Decision No. 61730, June 4, 1999).

A more relevant criterion to analyze would be how many Commission-regulated, users of electric energy still use an adjustor mechanism to pass changes in electricity costs to their customers. This analysis would demonstrate that the ability to adjust one's rates to cover changes in costs to purchase power is a necessary element of rate design. Another relevant criterion Staff should have analyzed is how many providers of electric energy have the ability to change their retail rates without a full and complete rate case due to the use of adjustor mechanisms, significantly affecting the costs to purchase power by larger retail users such as Arizona Water.

Q. HAS THE COMPANY PERFORMED SUCH AN ANALYSIS?

A. Yes, and the result of the Company's analysis is that at least fifty percent of the regulated electric utilities listed on the Commission's website still have purchased power adjustment mechanisms in their filed tariffs. These entities have the ability to adjust their retail electric rates to reflect changes in purchased power costs on a monthly basis without Commission approval. An example is provided at page 3 of Exhibit SLH-R3. Of the seven Commission-regulated gas utilities, all appear to have adjustor mechanisms in their tariffs, again, with the ability to adjust their retail rates on a monthly basis without Commission approval. It was also determined that there has been no concerted attempt by Staff to eliminate those adjustor mechanisms from the rate design of those entities. The Company's PPAM should not be eliminated either. Electric and gas adjustor mechanisms do not require prior Commission approval before being placed into effect. The Commission may consider modifying the mechanism to eliminate the requirement for Commission approval of the changes in the adjustor factors.

C. Purchased Water Adjustment Mechanism

Q. STAFF ALSO RECOMMENDS ELIMINATION OF THE PURCHASED WATER ADJUSTOR MECHANISM ALTOGETHER. DOES THE COMPANY AGREE WITH THIS RECOMMENDATION?

A. No, the Company does not agree that the purchased water adjustment mechanism ("PWAM") should be eliminated. Mr. Ludders discusses the Company's purchased water adjustment mechanism for the Ajo, San Manuel and Superior systems in his direct testimony. *See* Ludders Direct at 11, ls. 12-21. Of course, as a starting point, any discussion of eliminating the adjustor mechanism for the Company's Ajo system is outside this Eastern Group rate case because the Ajo system is part of the Company's Western Group systems.

Regarding the recommendation to eliminate the PWAM for the San Manuel and Superior systems, the Company opposes Staff's recommendation. In the San Manuel system, during the test year, purchased water expense was twenty-nine percent (29%) of that systems' operations and maintenance expenses. The last two increases by BHP increased the cost of purchased water from $.57 to $1.12, a ninety-six percent (96%) increase. The price that Arizona Water pays to purchase water for its San Manuel system is set by BHP and outside the control of the Company or the Commission because BHP in not a public utility. Even when the Company attempted to obtain a legal remedy to obtain a more reasonable price for the purchased water, BHP prevailed. As a consequence, eliminating the PWAM from the San Manuel system would expose the Company to increased risk from large, uncontrollable operating expense increases.

Assuming that the recommended two-step consolidation of the Superior and Apache Junction systems is approved, the Superior PWAM would be eliminated in the next rate proceeding when a common commodity cost is developed for both systems.

Q. **HAS THE COMMISSION ADDRESSED THE QUESTION OF MODIFYING THE PURCHASED POWER AND PURCHASED WATER ADJUSTOR MECHANISMS IN PAST ARIZONA WATER COMPANY RATE MAKING DOCKETS?**

A. Yes. In Commission Decision No. 58120 (December 23, 1992), the Commission rejected Staff's recommended change in the thresholds for obtaining an adjustment in the PPAM and PWAM, stating:

> If purchased power and/or water costs are trending upward, gradually recognizing those increasing costs through incremental rate adjustments sends a more appropriate price signal to users and receives greater customer acceptance than the less frequent, but far larger, rate increases contemplated in Staff's proposal. If purchased power and/or water costs are trending downward, Staff's proposal would delay the refund owing to customers. We believe these customer interests are best served by retaining the existing thresholds.

See Decision No. 58120 at 30, l. 20 through 31 at l. 1. This rationale has not changed and the Company urges the Commission to maintain the Company's existing adjustor mechanisms.

D. Central Arizona Project Cost Amortization

Q. **ON JUNE 19, 2003, CAWCD ADOPTED THE FINAL 2004 WATER RATE SCHEDULE THAT CONTAINS CAP CAPITAL AND DELIVERY**

CHARGES FOR 2004. SHOULD THESE CAP CAPITAL AND DELIVERY CHARGES BE INCORPORATED IN THE COMPANY'S OPERATING EXPENSES IN THIS PROCEEDING?

A. Yes. To properly compute operating results for the period that the rates resulting from this proceeding will be in effect, known and measurable changes in the M&I charge and CAP delivery charges must be incorporated. The M&I charge of $74 per acre foot ("AF") adopted on June 19, 2003 by the CAWCD compares to the $66 per AF proposed by the Company and accepted by Staff in its filing. Since the $74 per AF rate is a known and measurable change, an adjustment should be made to the Company's operating expenses. The amount of the adjustment due to the change in the M&I rate per AF is an additional increase of $16,520 (2065 AF X ($74-$66)) in the M&I charges over that already reflected in the Company's and Staff's proposals.

The delivery charge was also revised to $32 per AF from the test year level of $43 per AF. The effect of this concurrent known and measurable change, recognized by both Staff and RUCO, neither of which picked up the change in the M&I charge, is a decrease of $22,715 (2065 AF X ($32-$43)) in the delivery ~~charges for water delivered to the Mesa Treatment Plant. The effect of recognizing~~ these known and measurable changes in CAP purchased water expense is a net decrease of $6,195 ($16,520-$22,715) to the Staff's recommended level of $152,532 shown on Schedule REL-13 for Apache Junction.

Q. **SCHEDULE REL-13 FOR APACHE JUNCTION SUMMARIZES THE PURCHASED WATER EXPENSES FROM THE COMPANY'S FILING AND STAFF'S ADJUSTED LEVEL. ARE THE AMOUNTS SHOWN CORRECT?**

A. The total adjusted test year 2001 purchased water expense of $1,003,040 shown on the Company's Schedule C-1, line 2, for Apache Junction includes two pro forma adjustments. One is a pro forma adjustment to annualize purchased water costs of $166,225 (*See* Schedule C-2, page 6 of 36, line 7) and the second is a pro forma adjustment to annualize expenses for year-end customers in the amount of $31,604 (*See* Schedule C-2 page 5 of 36) totaling the $197,829 referred to in the testimony of Staff's witness Ronald E. Ludders on page 24. Staff has eliminated the $31,604 in error on its Schedule REL-13. Staff, on its Schedule REL-15, correctly addresses this portion of the Company's purchased water costs, but the effect of Staff's error is an understatement of its recommended purchased water expenses of $31,604.

E. Water Testing Expenses

Q. IS STAFF'S RECOMMENDED ADJUSTMENT TO THE COMPANY'S PROPOSED WATER TESTING EXPENSES TO REMOVE CHARGES FOR TESTING FOR RADIO-CHEMICALS APPROPRIATE?

A. Staff's Response to the Company's Data Request No. 5.1, copy attached as Exhibit SLH-R6, states that the costs for testing for radio-chemicals for new wells are more appropriately capitalized and included in the development costs of the well. Based upon this response, the Company will not oppose the Staff's recommended level of water testing costs which exclude testing for radio-chemicals for new wells which is not covered by the Monitoring Assistance Program ("MAP").

F. Rate Case Expense

Q. DOES THE COMPANY AGREE WITH STAFF'S RECOMMENDATIONS CONCERNING RATE CASE EXPENSE?

A. The Company strongly objects to Staff's recommendation to limit rate case expense to some arbitrary level estimated by Staff. It is somewhat ironic that Staff relies on the "known and measurable" concept when it reduced the Company's revenue requirement but proposes the use of "their estimates" at times when they wish to reduce the recovery of legitimate actual, known and measurable expenses. Staff's recommendation does not purport to use the amount of "known and measurable" rate case expense as of September 15 with an estimate of only the remaining costs. Instead, the basis of Staff's recommended level of rate case expense is premised, in large part, on a comparison of rate case expenses incurred in the Company's 1990 rate case versus the Northern Group's 1999 rate case and the estimate for this proceeding. In reaching this result, Staff ignores the significant differences between the 1990 and 1999 case and asks the Commission to assume they are using a valid comparison. Staff's comparison doesn't even rise to the level of "apples and oranges"; it is more of a "fruit and vegetable" comparison. In the 1990 rate case, which included all eighteen systems of Arizona Water Company, an in-house preparation and defense was utilized. In other words, there was no outside counsel or cost of capital witness. The Company's experience in that proceeding, coupled with the implementation of time clock rules with extremely short time periods for preparation of rebuttal and rejoinder testimony and the increasingly litigious nature of rate cases, particularly the increased reliance on formal data requests (over 200 served on the Company by Staff alone in this docket), it was determined that additional resources were necessary for processing future rate requests.

Ironically, outside services were retained to assist in preparing both the cost of capital and the legal defense of the Company's 1999 rate request and the Commission adopted the Company's proposed level of rate case expense.

In any event, it follows that a comparison to the situation more than a decade ago is not a valid comparison. Indeed, it is the Company's position that an estimate of the level of rate case expense must be evaluated on its individual merits and a determination of the appropriate amount of recovery to be authorized based thereon. The Staff has a data request, REL 25-2, setting forth an estimate of the cost of outside services through the final disposition of the rate case that will be updated on September 15, 2003. It is the Company's intention to update the current estimate of $274,550 at that time with actual "known and measurable" expenses including an allocation of the actual legal fees incurred in the Arsenic Cost Recovery Mechanism ("ACRM") proceeding, Phase Two of the Northern Group rate proceeding, which proceeding will benefit both the Northern and Eastern Group customers. In addition, the Company will provide a further updated estimate as soon as the billings for the hearings have been received.

Q. IS STAFF CORRECT IN ITS ASSUMPTION THAT HALF OF THE COMPANY'S ATTORNEYS' FEES ASSOCIATED WITH THIS RATE CASE WERE INCURRED AS OF APRIL 30, 2003?

A. No. Specifically, Staff estimates that half of the attorney fees were incurred as of April 30, 2003 because Staff characterized this date as the half way point of the rate case. *See* Ludders Direct at 13, ls. 10-27. However, as of April 30, 2003, the Company had not seen any of the other parties' filings, including Staff's hundred's of pages of direct testimony and schedules, had not yet conducted any discovery, and had not begun preparing its rebuttal filing. Moreover, no party has yet to submit a surrebuttal or rejoinder filing, not a single day of hearing has yet taken place and no post-hearing briefing has occurred. Frankly, as of April 30, 2003, something less than a third of the rate case activities had taken place and the bulk of work by attorneys (analyzing other parties' filings, preparing rebuttal and rejoinder, hearing and briefing) had not yet commenced.

In sum, Staff's claim that the Company has completed half this rate case, at least so far as its attorneys are involved, is without merit. Certainly a more sound basis for establishing the reasonableness of the Company's known and measurable rate case expenses must be offered before there is any basis to reduce the amount of the Company's requested rate case expense.

Q. DOES THE COMPANY AGREE WITH STAFF'S RECOMMENDED 5-YEAR AMORTIZATION OF RATE CASE EXPENSE?

A. No we do not. Instead, the Company continues to believe that an amortization period of three years is appropriate. There are many factors impacting the time a utility seeks rate relief and in volatile times such as we are experiencing with fluctuating costs of capital, increased need for capital investments and potential infrastructure improvements, and uncertainty of economic conditions, a three-year amortization could most likely match the period of time before Arizona Water must seek additional rate relief. Therefore, the Company maintains its request for a three-year amortization.

G. Additional CIAC Amortization

Q. IS THE STAFF PROPOSING AN ADJUSTMENT TO THE COMPANY'S CONTRIBUTIONS IN AID OF CONSTRUCTION ("CIAC") AMORTIZATION?

A. It appears that the Staff is calculating the amortization of CIAC at a composite depreciation rate and adjusting the Company's depreciation expense. *See* Ludders Direct at 32, ls. 2-5. As far as the Company can discern, a 2.34 percent rate has been applied to the test year-end balance of gross contributions for the Eastern Group of $7,850,910. This calculation is apparently intended to reflect the new level of CIAC amortizations that the Company should incur utilizing the component depreciation rates. If this is the intended purpose, the annual amortization should have been compared to the amount included in the Company's presentation, which is $185,965 on a total Eastern Group basis. In addition, a composite rate should have been developed using the annual depreciation associated with the plant accounts that include contributions. Those accounts are the Transmission and Distribution Mains, Fire Sprinkler Taps, Services, Meters, and Hydrants. A composite rate for the Eastern Group's contributed plant accounts is more appropriately 2.00% for this proceeding. Applying this figure to the CIAC balance of $7,850,910 results in a total Eastern Group amortization of $157,018 contrasted to the test year level of $185,965, an adjustment increasing the depreciation expense by $28,947 versus the Staff's adjustment, which reduces depreciation expense by $191,417 on a total Eastern Group Basis. Although not included in the Staff's direct filing, this adjustment to depreciation expense, for consistency purposes, should also be reflected as an adjustment to the CIAC balance reflected in Rate Base.

H. PCG Settlement-Net Operating Income Effects

Q. PLEASE EXPLAIN THE COMPANY'S ADJUSTMENTS TO REBUT STAFF'S RECOMMENDATION CONCERNING TREATMENT OF THE PCG SETTLEMENT?

A. To begin with, as explained by Mr. Garfield and quantified by Mr. Kennedy, Staff has completely ignored all of the benefits of the settlement already obtained for ratepayers in the Miami system. The Company correctly accounted for the settlement payment as Mr. Kennedy described in his testimony. To adopt the Company's rebuttal position as developed thoroughly in the Rebuttal Testimony of Mr. Garfield and Mr. Kennedy, a reversal of all PCG-related adjustments is necessary.

Q. DOES THIS CONCLUDE YOUR REBUTTAL TESTIMONY?

A. Yes, it does, except that I wish to note that my silence on any issue raised or recommendation made by Staff or RUCO should not be taken as the Company's acceptance of such issue or recommendation.

EXHIBITS

Arizona Water Company
ORIGINAL COST RATE BASE - NET PLANT
END OF TEST YEAR 2001

			Eastern Group		
Line No.	Description	AWC's Adjusted TY (As Filed) (a)	Staff's Adjusted TY (b)	Proposed Rebuttal Adjustments (c)	Rebuttal Adjusted TY (d)
1.	Gross Plant In Service	86,270,323	82,717,891	0	82,717,891
2.	Phoenix Office Allocation	1,639,085	177,640	1,581,093	1,758,733
3.	Meter Shop Allocation	34,141	3,999	34,140	38,139
4.	Total Gross Plant In Service	87,943,549	82,899,530	1,615,233	84,514,764
5.	less: Accumulated Depreciation	(18,321,740)	(19,835,625)	1,678,091	(18,157,533)
6.	Net Plant In Service	69,621,810	63,063,906	3,293,325	66,357,231
7.	Construction Work In Progress	0	0	0	0
8.	Total Net Plant	69,621,810	63,063,906	3,293,325	66,357,231

Arizona Water Company
ORIGINAL COST RATE BASE - NET PLANT
END OF TEST YEAR 2001

Line No.	Description	AWC's Adjusted TY (As Filed) (a)	Apache Junction Staff's Adjusted TY (b)	Proposed Rebuttal Adjustments (c)	Rebuttal Adjusted TY (d)	
1.	Gross Plant In Service	55,226,791	51,814,226	0	51,814,226	(a)
2.	Phoenix Office Allocation	852,453	86,619	822,293	908,912	
3.	Meter Shop Allocation	17,756	1,960	17,756	19,716	
4.	Total Gross Plant In Service	56,097,000	51,902,805	840,049	52,742,854	
5.	less: Accumulated Depreciation	(8,791,705)	(9,892,252)	1,299,493	(8,592,759)	
6.	Net Plant In Service	47,305,295	42,010,553	2,139,542	44,150,095	
7.	Construction Work In Progress	0	0	0	0	
8.	Total Net Plant	47,305,295	42,010,553	2,139,542	44,150,095	

(a) - $704,903 removed from Gross Plant in Service for Unamortized CAP to be shown as separate item on Rate Base Schedule.

Arizona Water Company
ORIGINAL COST RATE BASE - NET PLANT
END OF TEST YEAR 2001

Line No.	Description	AWC's Adjusted TY (As Filed) (a)	Bisbee Staff's Adjusted TY (b)	Proposed Rebuttal Adjustments (c)	Rebuttal Adjusted TY (d)
1.	Gross Plant In Service	7,433,939	7,613,913	0	7,613,913
2.	Phoenix Office Allocation	189,951	19,301	183,230	202,531
3.	Meter Shop Allocation	3,956	436	3,956	4,392
4.	Total Gross Plant In Service	7,627,846	7,633,650	187,186	7,820,837
5.	less: Accumulated Depreciation	(3,099,049)	(3,228,015)	116,066	(3,111,949)
6.	Net Plant In Service	4,528,797	4,405,635	303,253	4,708,888
7.	Construction Work In Progress	0	0	0	0
8.	Total Net Plant	4,528,797	4,405,635	303,253	4,708,888

Arizona Water Company
ORIGINAL COST RATE BASE - NET PLANT
END OF TEST YEAR 2001

Miami

Line No.	Description	AWC's Adjusted TY (As Filed) (a)	Staff's Adjusted TY (b)	Proposed Rebuttal Adjustments (c)	Rebuttal Adjusted TY (d)
1.	Gross Plant In Service				
2.	Phoenix Office Allocation	6,837,666	6,770,808	(0)	6,770,808
3.	Meter Shop Allocation	193,170	19,629	186,336	205,965
		4,024	444	4,024	4,468
4.	Total Gross Plant In Service	7,034,860	6,790,881	190,359	6,981,240
5.	less: Accumulated Depreciation	(1,713,977)	(1,745,153)	23,278	(1,721,875)
6.	Net Plant In Service	5,320,883	5,045,728	213,637	5,259,365
7.	Construction Work In Progress	0	0	0	0
8.	Total Net Plant	5,320,883	5,045,728	213,637	5,259,365

Arizona Water Company
ORIGINAL COST RATE BASE - NET PLANT
END OF TEST YEAR 2001

Line No.	Description	AWC's Adjusted TY (As Filed) (a)	Oracle Staff's Adjusted TY (b)	Proposed Rebuttal Adjustments (c)	Rebuttal Adjusted TY (d)
1.	Gross Plant In Service	5,179,022	5,064,631	(0)	5,064,631
2.	Phoenix Office Allocation	93,008	9,452	89,717	99,169
3.	Meter Shop Allocation	1,937	214	1,937	2,151
4.	Total Gross Plant In Service	5,273,967	5,074,297	91,654	5,165,951
5.	less: Accumulated Depreciation	(1,468,545)	(1,570,314)	97,821	(1,472,493)
6.	Net Plant In Service	3,805,422	3,503,983	189,475	3,693,458
7.	Construction Work In Progress	0	0	0	0
8.	Total Net Plant	3,805,422	3,503,983	189,475	3,693,458

Arizona Water Company
ORIGINAL COST RATE BASE - NET PLANT
END OF TEST YEAR 2001

Line No.	Description	AWC's Adjusted TY (As Filed) (a)	San Manuel Staff's Adjusted TY (b)	Proposed Rebuttal Adjustments (c)	Rebuttal Adjusted TY (d)
1.	Gross Plant In Service	1,554,600	1,514,841	(0)	1,514,841
2.	Phoenix Office Allocation	79,057	8,033	76,260	84,293
3.	Meter Shop Allocation	1,647	182	1,647	1,829
4.	Total Gross Plant In Service	1,635,304	1,523,056	77,907	1,600,962
5.	less: Accumulated Depreciation	(736,074)	(708,955)	(27,313)	(736,268)
6.	Net Plant In Service	899,231	814,102	50,593	864,694
7.	Construction Work In Progress	0	0	0	0
8.	Total Net Plant	899,231	814,102	50,593	864,694

Arizona Water Company
ORIGINAL COST RATE BASE - NET PLANT
END OF TEST YEAR 2001

			Sierra Vista		
Line No.	Description	AWC's Adjusted TY (As Filed) (a)	Staff's Adjusted TY (b)	Proposed Rebuttal Adjustments (c)	Rebuttal Adjusted TY (d)
1.	Gross Plant In Service	5,282,359	5,219,293	0	5,219,293
2.	Phoenix Office Allocation	130,569	13,267	125,949	139,216
3.	Meter Shop Allocation	2,720	300	2,720	3,020
4.	Total Gross Plant In Service	5,415,648	5,232,860	128,669	5,361,529
5.	less: Accumulated Depreciation	(1,406,900)	(1,499,622)	89,077	(1,410,545)
6.	Net Plant In Service	4,008,748	3,733,238	217,746	3,950,984
7.	Construction Work In Progress	0	0	0	0
8.	Total Net Plant	4,008,748	3,733,238	217,746	3,950,984

Arizona Water Company
ORIGINAL COST RATE BASE - NET PLANT
END OF TEST YEAR 2001

Line No.	Description	AWC's Adjusted TY (As Filed) (a)	Superior Staff's Adjusted TY (b)	Proposed Rebuttal Adjustments (c)	Rebuttal Adjusted TY (d)
1.	Gross Plant In Service	4,327,525	4,299,052	0	4,299,052
2.	Phoenix Office Allocation	89,788	9,123	86,612	95,735
3.	Meter Shop Allocation	1,870	207	1,870	2,077
4.	Total Gross Plant In Service	4,419,183	4,308,382	88,482	4,396,864
5.	less: Accumulated Depreciation	(986,086)	(1,066,976)	76,079	(990,897)
6.	Net Plant In Service	3,433,097	3,241,406	164,561	3,405,967
7.	Construction Work In Progress	0	0	0	0
8.	Total Net Plant	3,433,097	3,241,406	164,561	3,405,967

Arizona Water Company
ORIGINAL COST RATE BASE - NET PLANT
END OF TEST YEAR 2001

Line No.	Description	AWC's Adjusted TY (As Filed) (a)	Winkelman Staff's Adjusted TY (b)	Proposed Rebuttal Adjustments (c)	Rebuttal Adjusted TY (d)
1.	Gross Plant In Service	428,421	421,127	0	421,127
2.	Phoenix Office Allocation	11,089	12,216	10,697	22,913
3.	Meter Shop Allocation	231	256	231	487
4.	Total Gross Plant In Service	439,741	433,599	10,928	444,527
5.	less: Accumulated Depreciation	(119,404)	(124,338)	3,590	(120,748)
6.	Net Plant In Service	320,337	309,261	14,519	323,780
7.	Construction Work In Progress	0	0	0	0
8.	Total Net Plant	320,337	309,261	14,519	323,780

Arizona Water Company
ORIGINAL COST RATE BASE
END OF TEST YEAR 2001

Line No.	Description	AWC's Adjusted TY (As Filed) (a)	Eastern Group Staff's Adjusted TY (b)	Proposed Rebuttal Adjustments (c)	Rebuttal Adjusted TY (d)
1.	Gross Plant In Service	86,270,323	82,717,891	0	82,717,891
2.	Phoenix Office Allocation	1,639,085	177,640	1,581,093	1,758,733
3.	Meter Shop Allocation	34,141	3,999	34,140	38,139
4.	Total Gross Plant In Service	87,943,549	82,899,530	1,615,233	84,514,764
5.	less: Accumulated Depreciation	(18,321,740)	(19,835,625)	1,678,091	(18,157,533)
6.	Net Plant In Service	69,621,810	63,063,906	3,293,325	66,357,231
7.	Construction Work In Progress	0	0	0	0
8.	Total Net Plant	69,621,810	63,063,906	3,293,325	66,357,231
9.	Less: Customers' Advances for Construction	(17,232,663)	(17,232,663)	0	(17,232,663)
10.	Contributions in Aid of Construction.				
11.	Gross	(7,850,910)	(7,850,910)	0	(7,850,910)
12	Accumulated Amortization	968,440	968,440	(28,947)	939,493
13.	Net Contributions In Aid Of Construction	(24,115,133)	(24,115,133)	(28,947)	(24,144,080)
14.	Deferred Income Tax	(4,825,667)	(4,825,667)	0	(4,825,667)
15.	Deferred CAP (Net)	0	684,785	6,737	691,522
16.	Add: Total Working Capital Allowance (b)	923,870	(1,054,873)	1,978,743	923,870
17.	Total Rate Base Components & Adjustments	41,604,880	33,753,018	5,249,858	39,002,876
18.	PCG Settlement	0	(1,350,000)	1,350,000	0
19.	Total Rate Base Components & Adjustments & PCG	41,604,880	32,403,018	6,599,858	39,002,876

Arizona Water Company
ORIGINAL COST RATE BASE
END OF TEST YEAR 2001

Line No.	Description	AWC's Adjusted TY (As Filed) (a)	Apache Junction Staff's Adjusted TY (b)	Proposed Rebuttal Adjustments (c)	Rebuttal Adjusted TY (d)	
1.	Gross Plant In Service	55,226,791	51,814,226	0	51,814,226	(a)
2.	Phoenix Office Allocation	852,453	86,619	822,293	908,912	
3.	Meter Shop Allocation	17,756	1,960	17,756	19,716	
4.	Total Gross Plant In Service	56,097,000	51,902,805	840,049	52,742,854	
5.	less: Accumulated Depreciation	(8,791,705)	(9,892,252)	1,299,493	(8,592,759)	
6.	Net Plant In Service	47,305,295	42,010,553	2,139,542	44,150,095	
7.	Construction Work In Progress	0	0	0	0	
8.	Total Net Plant	47,305,295	42,010,553	2,139,542	44,150,095	
9.	Less: Customers' Advances for Construction	(15,443,377)	(15,443,377)	0	(15,443,377)	
10.	Contributions In Aid of Construction					
11.	Gross	(6,228,486)	(6,228,486)	0	(6,228,486)	
12	Accumulated Amortization	713,806	713,806	(21,017)	692,789	
13.	Net Contributions In Aid Of Construction	(20,958,057)	(20,958,057)	(21,017)	(20,979,074)	
14.	Deferred Income Tax	(2,699,309)	(2,699,309)	0	(2,699,309)	
15.	Deferred CAP (Net)	0	684,785	6,737	691,522	(a)
16.	Add: Total Working Capital Allowance (b)	559,087	(691,907)	1,250,994	559,087	
17.	Total Rate Base Components & Adjustments	24,207,016	18,346,065	3,376,255	21,722,320	

(a) - $704,903 removed from Gross Plant In Service for Unamortized CAP to be shown as separate item on Rate Base Schedule.

Arizona Water Company
ORIGINAL COST RATE BASE
END OF TEST YEAR 2001

Line No.	Description	AWC's Adjusted TY (As Filed) (a)	Bisbee Staff's Adjusted TY (b)	Proposed Rebuttal Adjustments (c)	Rebuttal Adjusted TY (d)
1.	Gross Plant In Service	7,433,939	7,613,913	0	7,613,913
2.	Phoenix Office Allocation	189,951	19,301	183,230	202,531
3.	Meter Shop Allocation	3,956	436	3,956	4,392
4.	Total Gross Plant In Service	7,627,846	7,633,650	187,186	7,820,837
5.	less: Accumulated Depreciation	(3,099,049)	(3,228,015)	116,066	(3,111,949)
6.	Net Plant In Service	4,528,797	4,405,635	303,253	4,708,888
7.	Construction Work In Progress	0	0	0	0
8.	Total Net Plant	4,528,797	4,405,635	303,253	4,708,888
9.	Less: Customers' Advances for Construction	(190,083)	(190,083)	0	(190,083)
10.	Contributions in Aid of Construction				
11.	Gross	(372,133)	(372,133)	0	(372,133)
12	Accumulated Amortization	55,613	55,613	(1,209)	54,404
13.	Net Contributions In Aid Of Construction	(506,603)	(506,603)	(1,209)	(507,812)
14.	Deferred Income Tax	(423,066)	(423,066)	0	(423,066)
15.	Deferred CAP (Net)	0	0	0	0
16.	Add: Total Working Capital Allowance (b)	100,985	(50,285)	151,270	100,985
17.	Total Rate Base Components & Adjustments	3,700,113	3,425,681	453,313	3,878,995

Arizona Water Company
ORIGINAL COST RATE BASE
END OF TEST YEAR 2001

Line No.	Description	AWC's Adjusted TY (As Filed) (a)	Miami Staff's Adjusted TY (b)	Proposed Rebuttal Adjustments (c)	Rebuttal Adjusted TY (d)
1.	Gross Plant In Service	6,837,666	6,770,808	(0)	6,770,808
2.	Phoenix Office Allocation	193,170	19,629	186,336	205,965
3.	Meter Shop Allocation	4,024	444	4,024	4,468
4.	Total Gross Plant In Service	7,034,860	6,790,881	190,359	6,981,240
5.	less: Accumulated Depreciation	(1,713,977)	(1,745,153)	23,278	(1,721,875)
6.	Net Plant In Service	5,320,883	5,045,728	213,637	5,259,365
7.	Construction Work In Progress	0	0	0	0
8.	Total Net Plant	5,320,883	5,045,728	213,637	5,259,365
9.	Less: Customers' Advances for Construction	(109,428)	(109,428)	0	(109,428)
10.	Contributions In Aid of Construction				
11.	Gross	(188,394)	(188,394)	0	(188,394)
12	Accumulated Amortization	32,086	32,086	(1,061)	31,025
13.	Net Contributions In Aid Of Construction	(265,736)	(265,736)	(1,061)	(266,797)
14.	Deferred Income Tax	(566,719)	(566,719)	0	(566,719)
15.	Deferred CAP (Net)	0	0	0	0
16.	Add: Total Working Capital Allowance (b)	81,768	(122,661)	204,429	81,768
17.	Total Rate Base Components & Adjustments	4,570,196	4,090,612	417,005	4,507,617
18.	PCG Settlement	0	(1,350,000)	1,350,000	0
19.	Total Rate Base Components & Adjustments & PCG	4,570,196	2,740,612	1,767,005	4,507,617

Arizona Water Company
ORIGINAL COST RATE BASE
END OF TEST YEAR 2001

Oracle

Line No.	Description	AWC's Adjusted TY (As Filed) (a)	Staff's Adjusted TY (b)	Proposed Rebuttal Adjustments (c)	Rebuttal Adjusted TY (d)
1.	Gross Plant In Service	5,179,022	5,064,631	(0)	5,064,631
2.	Phoenix Office Allocation	93,008	9,452	89,717	99,169
3.	Meter Shop Allocation	1,937	214	1,937	2,151
4.	Total Gross Plant In Service	5,273,967	5,074,297	91,654	5,165,951
5.	less: Accumulated Depreciation	(1,468,545)	(1,570,314)	97,821	(1,472,493)
6.	Net Plant In Service	3,805,422	3,503,983	189,475	3,693,458
7.	Construction Work In Progress	0	0	0	0
8.	Total Net Plant	3,805,422	3,503,983	189,475	3,693,458
9.	Less: Customers' Advances for Construction	(473,356)	(473,356)	0	(473,356)
10.	Contributions in Aid of Construction				
11.	Gross	(258,151)	(258,151)	0	(258,151)
12	Accumulated Amortization	37,740	37,740	(1,225)	36,515
13.	Net Contributions In Aid Of Construction	(693,767)	(693,767)	(1,225)	(694,992)
14.	Deferred Income Tax	(344,341)	(344,341)	0	(344,341)
15.	Deferred CAP (Net)	0	0	0	0
16.	Add: Total Working Capital Allowance (b)	52,086	(50,607)	102,693	52,086
17.	Total Rate Base Components & Adjustments	2,819,400	2,415,268	290,943	2,706,211

Arizona Water Company
ORIGINAL COST RATE BASE
END OF TEST YEAR 2001

			San Manuel		
Line No.	Description	AWC's Adjusted TY (As Filed) (a)	Staff's Adjusted TY (b)	Proposed Rebuttal Adjustments (c)	Rebuttal Adjusted TY (d)
1.	Gross Plant In Service	1,554,600	1,514,841	(0)	1,514,841
2.	Phoenix Office Allocation	79,057	8,033	76,260	84,293
3.	Meter Shop Allocation	1,647	182	1,647	1,829
4.	Total Gross Plant In Service	1,635,304	1,523,056	77,907	1,600,962
5.	less: Accumulated Depreciation	(736,074)	(708,955)	(27,313)	(736,268)
6.	Net Plant In Service	899,231	814,102	50,593	864,694
7.	Construction Work In Progress	0	0	0	0
8.	Total Net Plant	899,231	814,102	50,593	864,694
9.	Less: Customers' Advances for Construction	(23,194)	(23,194)	0	(23,194)
10.	Contributions in Aid of Construction				
11.	Gross	(20,375)	(20,375)	0	(20,375)
12	Accumulated Amortization	2,990	2,990	46	3,036
13.	Net Contributions In Aid Of Construction	(40,579)	(40,579)	46	(40,534)
14.	Deferred Income Tax	(93,372)	(93,372)	0	(93,372)
15.	Deferred CAP (Net)	0	0	0	0
16.	Add: Total Working Capital Allowance (b)	28,714	(38,700)	67,414	28,714
17.	Total Rate Base Components & Adjustments	793,994	641,451	118,053	759,503

Arizona Water Company
ORIGINAL COST RATE BASE
END OF TEST YEAR 2001

Line No.	Description	AWC's Adjusted TY (As Filed) (a)	Sierra Vista Staff's Adjusted TY (b)	Proposed Rebuttal Adjustments (c)	Rebuttal Adjusted TY (d)
1.	Gross Plant In Service	5,282,359	5,219,293	0	5,219,293
2.	Phoenix Office Allocation	130,569	13,267	125,949	139,216
3.	Meter Shop Allocation	2,720	300	2,720	3,020
4.	Total Gross Plant In Service	5,415,648	5,232,860	128,669	5,361,529
5.	less: Accumulated Depreciation	(1,406,900)	(1,499,622)	89,077	(1,410,545)
6.	Net Plant In Service	4,008,748	3,733,238	217,746	3,950,984
7.	Construction Work In Progress	0	0	0	0
8.	Total Net Plant	4,008,748	3,733,238	217,746	3,950,984
9.	Less: Customers' Advances for Construction	(587,611)	(587,611)	0	(587,611)
10.	Contributions in Aid of Construction				
11.	Gross	(699,448)	(699,448)	0	(699,448)
12	Accumulated Amortization	113,980	113,980	(4,045)	109,935
13.	Net Contributions In Aid Of Construction	(1,173,079)	(1,173,079)	(4,045)	(1,177,124)
14.	Deferred Income Tax	(331,421)	(331,421)	0	(331,421)
15.	Deferred CAP (Net)	0	0	0	0
16.	Add: Total Working Capital Allowance (b)	70,439	(28,293)	98,732	70,439
17.	Total Rate Base Components & Adjustments	2,574,687	2,200,445	312,433	2,512,878

Arizona Water Company
ORIGINAL COST RATE BASE
END OF TEST YEAR 2001

Line No.	Description	AWC's Adjusted TY (As Filed) (a)	Superior Staff's Adjusted TY (b)	Proposed Rebuttal Adjustments (c)	Rebuttal Adjusted TY (d)
1.	Gross Plant In Service				
2.	Phoenix Office Allocation	4,327,525	4,299,052	0	4,299,052
3.	Meter Shop Allocation	89,788	9,123	86,612	95,735
		1,870	207	1,870	2,077
4.	Total Gross Plant In Service	4,419,183	4,308,382	88,482	4,396,864
5.	less: Accumulated Depreciation	(986,086)	(1,066,976)	76,079	(990,897)
6.	Net Plant In Service	3,433,097	3,241,406	164,561	3,405,967
7.	Construction Work In Progress	0	0	0	0
8.	Total Net Plant	3,433,097	3,241,406	164,561	3,405,967
9.	Less: Customers' Advances for Construction	(384,759)	(384,759)	0	(384,759)
10.	Contributions in Aid of Construction				
11.	Gross	(82,088)	(82,088)	0	(82,088)
12	Accumulated Amortization	11,961	11,961	(423)	11,538
13.	Net Contributions In Aid Of Construction	(454,886)	(454,886)	(423)	(455,309)
14.	Deferred Income Tax	(332,521)	(332,521)	0	(332,521)
15.	Deferred CAP (Net)	0	0	0	0
16.	Add: Total Working Capital Allowance (b)	27,886	(53,426)	81,312	27,886
17.	Total Rate Base Components & Adjustments	2,673,576	2,400,573	245,450	2,646,023

Arizona Water Company
ORIGINAL COST RATE BASE
END OF TEST YEAR 2001

Line No.	Description	AWC's Adjusted TY (As Filed) (a)	Winkelman Staff's Adjusted TY (b)	Proposed Rebuttal Adjustments (c)	Rebuttal Adjusted TY (d)
1.	Gross Plant In Service	428,421	421,127	0	421,127
2.	Phoenix Office Allocation	11,089	12,216	10,697	22,913
3.	Meter Shop Allocation	231	256	231	487
4.	Total Gross Plant In Service	439,741	433,599	10,928	444,527
5.	less: Accumulated Depreciation	(119,404)	(124,338)	3,590	(120,748)
6.	Net Plant In Service	320,337	309,261	14,519	323,780
7.	Construction Work In Progress	0	0	0	0
8.	Total Net Plant	320,337	309,261	14,519	323,780
9.	Less: Customers' Advances for Construction	(20,855)	(20,855)	0	(20,855)
10.	Contributions In Aid of Construction				
11.	Gross	(1,835)	(1,835)	0	(1,835)
12	Accumulated Amortization	264	264	(11)	253
13.	Net Contributions In Aid Of Construction	(22,426)	(22,426)	(11)	(22,437)
14.	Deferred Income Tax	(34,918)	(34,918)	0	(34,918)
15.	Deferred CAP (Net)	0	0	0	0
16.	Add: Total Working Capital Allowance (b)	2,905	(18,994)	21,899	2,905
17.	Total Rate Base Components & Adjustments	265,898	232,923	36,406	269,329

CENTENNIAL SRP 1903 - 2003

P. O. Box 52025
Phoenix, Arizona 85072-2025

RECEIVED
OCT 22 2002
ARIZONA WATER COMPANY
PHOENIX - EXECUTIVE

October 18, 2002

Mr. Bill Garfield
Arizona Water Company
3805 N Black Canyon Hwy
Phoenix, AZ 85038-9006

Dear Bill,

SRP has incurred unanticipated fuel and purchased power costs in providing electricity to its retail customers during the first quarter of SRP's fiscal year (May 2002 through July 2002). These increased costs were precipitated by the purchase of power to replace generation units that have been curtailed or on outage. For example, SRP's hydro generation has been substantially reduced due to the drought, and certain local generating units have been on extended outage due to mechanical difficulties.

As a result, SRP's Board of Directors considered a management proposal to increase the Fuel and Purchased Power Adjustment Factor at a meeting held on Thursday, October 17, 2002. Management proposed establishing an adjustment factor of $0.00180/kWh applicable to all customer bills, and the Board agreed to this change.

This review of the Fuel and Purchased Power Adjustment Factor is in accordance with established procedures followed by the SRP Board of Directors and does not constitute a change to SRP's standard electric price plans. This change is effective with customer electric bills dated on or after November 1, 2002, concurrent with the implementation of winter base prices, which are substantially lower than summer base prices. As a result, we anticipate that most customers will see their bills decline over the winter billing season (November 2002 through April 2003).

Changes in the fuel and purchased power adjustment factor reflect solely actual fuel and purchased power costs, estimated future fuel and purchased power costs and the operational performance of generation units. The unanticipated fuel and purchased power costs are planned for collection over an 18-month period to minimize impacts on our customers.

While this change will affect your monthly electric bills, SRP also is undertaking measures to reduce fuel and other operating costs in the future. Further, SRP will continue to review fuel and purchased power costs on a quarterly basis and may propose to revise or eliminate the adjustment at a later date.

Even with this change, SRP's prices will continue to be among the lowest in Arizona and in the Southwest. If you have any questions, please contact your Account Manager, Mike G. Sullivan at 602.236.5708.

Sincerely,

Scott A Trout

Scott A. Trout
Manager, Commercial Customer Services

Navopache Electric Cooperative Bills now Unbundled

The Arizona Corporation Commission has requested that electric utilities unbundle their bills. Unbundling is the breakdown of the bills into components of electric service and related service charges such as generation, meter reading and billing, etc. Navopache Electric Cooperative has opted to do this as of your February billing. Below you will find a layout of the different charges and descriptions relating to these charges.

Distribution Charges:

Fixed Monthly Charge
Metering Charge
Meter Reading Charge
Billing Charge
Electricity Charge
Environmental Surcharge
Public Benefits Charge
CTC (Stranded Cost)

Total Distribution Charges

Generation Charges:

Electricity Charge
Power Cost Adjustment

Total Generation Charges

Service & Other Charges:

Deposit Applied
Establishment Fee

Total Other Services

Previous Balance:
Payments Received:
Balance Forward:
Total Distribution Charges:
Total Generation Charges:
Total Services & Other Charges:
Taxes:

Definitions

Distribution Charges – Charges directly related to the delivery of electric service to residential or business users. The Distribution Charges are based on the monthly energy usage to pay costs to build and operate the system.

Fixed Monthly Charge – The Customer Service Charge. This charge varies depending on the type of service. Where it is necessary to extend or reinforce existing distribution facilities, the minimum monthly charge may be increased to assure adequate compensation for the added facilities.

Metering Charge, Meter Reading Charge and Billing Charge – These charges are for providing these functions each month for the membership.

Electricity Charge – The consumer rate for kWh distributed.

Environmental Surcharge – Is paid by all electric utility consumers. This fee goes to a fund to help develop renewable resources.

Public Benefits Charge – Adder to help offset the costs associated with Navopache programs designed to promote load management and mandated by the Arizona Corporation Commission.

CTC (Competitive Transition Adjustment Charge, also referred to as stranded costs) – Based on your monthly energy usage, this goes to pay some of the costs for investments in power plants that were made under regulation.

<u>Generation Charges</u> – Charges associated with generation.

Electricity Charge – Consumer rate for kWh generated

Power Cost Adjustment – Factored in when the purchased power cost is increased or decreased beyond the base purchase power cost for every kilowatt hour sold. This difference is then passed on to all classes of consumers. While it can fluctuate on a monthly basis, the Power Cost Adjustment fctor has been a credit to consumers for quite some time. It has been responsible for the especially low winter bills this season.

Service & Other Charges – The fees that fall under this category are miscellaneous energy charges such as: deposit (refunded or assessed); establishment fee; check reading fee; reconnect fee; meter test fee; etc.

The new billing will also show the previous balance, payments received and the balance forward. This additional information is a welcome change and will provide easier accounting for our members.

Arizona Water Company
Analysis of PPAMs and PWAMs

	M-Gallons Sold 2001	Conversion to 100-Gallons	Effective 07/01/2003		Effect on 2001 Test Year Levels		Total
			PPAM Rates	PWAM Rates	PPAM Rates	PWAM Rates	PPAM & PWAM
Apache Junction	2,283,704.4	22,837,044.0	(0.0010)	0.0000	(22,837.04)	0.00	(22,837.04)
Bisbee	299,129.8	2,991,298.0	(0.0070)	0.0000	(20,939.09)	0.00	(20,939.09)
Sierra Vista	345,613.6	3,456,136.0	0.0000	0.0000	0.00	0.00	0.00
Casa Grande	3,185,006.3	31,850,063.0	(0.0010)	0.0000	(31,850.06)	0.00	(31,850.06)
Stanfield	30,942.3	309,423.0	(0.0040)	0.0000	(1,237.69)	0.00	(1,237.69)
White Tank	185,738.8	1,857,388.0	(0.0040)	0.0000	(7,429.55)	0.00	(7,429.55)
Ajo	55,672.6	556,726.0	0.0000	0.0000	0.00	0.00	0.00
Coolidge	438,791.0	4,387,910.0	0.0000	0.0000	0.00	0.00	0.00
Lakeside	259,834.2	2,598,342.0	(0.0270)	0.0000	(70,155.23)	0.00	(70,155.23)
Overgaard	101,494.4	1,014,944.0	(0.0140)	0.0000	(14,209.22)	0.00	(14,209.22)
Miami	310,124.4	3,101,244.0	(0.0060)	0.0000	(18,607.46)	0.00	(18,607.46)
San Manuel	214,845.7	2,148,457.0	(0.0020)	0.0760	(4,296.91)	163,282.73	158,985.82
Oracle	106,216.5	1,062,165.0	0.0030	0.0000	3,186.50	0.00	3,186.50
Winkelman	49,612.5	496,125.0	(0.0010)	0.0000	(496.13)	0.00	(496.13)
Sedona	971,086.1	9,710,861.0	(0.0010)	0.0000	(9,710.86)	0.00	(9,710.86)
Pinewood	83,797.7	837,977.0	(0.0010)	0.0000	(837.98)	0.00	(837.98)
Rimrock	87,115.9	871,159.0	0.0000	0.0000	0.00	0.00	0.00
Superior	110,459.0	1,104,590.0	0.0010	0.0000	1,104.59	0.00	1,104.59
Total Company	9,119,185.2	91,191,852.0			(198,316.13)	163,282.73	(35,033.40)

Arizona Corporation Commission
WORKING GROUP REPORTS

Attachment D

Proposed Policy for Central Arizona Project (CAP) Cost Recovery

The consensus of the CAP Working Group is that the Arizona Corporation Commission (Commission) should encourage water companies to retain their Central Arizona Project (CAP) water allocation. The purpose is to allow water companies to accomplish long term planning of their water resource needs for the benefit of their customers. The consensus of the group was that the Commission should accomplish this encouragement as follows:

1. A water company would be allowed to recover CAP costs if it could demonstrate that it needed the CAP allocation to properly serve its customers.
2. The water company must demonstrate that the need would occur by the year 2025.
3. The water company must demonstrate that it will actually be using a reasonable amount of its CAP allocation by 2025.
4. The water company must demonstrate that it will be using all of its CAP allocation by 2034.
5. "Use" will be those methods of using CAP water that are defined as "use" by the Arizona Department of Water Resources.
6. In order to obtain cost recovery, a water company must file a rate case and provide evidence demonstrating items 1 though 4 above.
7. At the time that cost recovery is approved for a water company, cost recovery will depend on how much of company's CAP allocation is actually being used -

    a. If none of the CAP allocation is actually being used, the company will be allowed to recover dollar for dollar its appropriate CAP expenses, without earning a rate of return. The cost recovery will be split between a charge in the commodity portion of the rate and a CAP Hook-up Fee. The charge in the commodity will be that amount needed to pay the M&I portion of the expense for that amount of CAP water equal to the amount of groundwater actually being used by the current customers. The CAP Hook-up Fee will be calculated as that portion needed to pay the remainder of the M&I charges. This is similar to the method used in the Vail Water Company rate case (Decision No. 62450). If the CAP Hook-up Fee is determined by the Commission to have to be excessive in order to recover all the CAP costs, the remainder should be deferred and collected later as the company grows and adds additional customers and/or the rate of growth increases to allow the collection of additional CAP Hook-up Fees.
    b. If only a portion of the CAP allotment is being used, cost recovery will be split. For that portion of the CAP allotment not being used, cost recovery will be allowed as explained above (#7a). For that portion of the CAP allotment actually being used, cost recovery will be as with any other used and useful item in a rate case, i.e., the plant needed will be included in rate base and earn a rate of return, while the M&I and OM&R expenses for

that portion of the CAP allotment will be recovered as any other expense.

c. When all the CAP allotment is being used, cost recovery will be as described in the second half above (#7b), i.e., just like any other plant and expense item that is used and useful.

d. For those water companies that have not obtained a specific accounting order from the Commission that details how CAP costs incurred up to this time would be treated and meet items 1 through 4 above, the actual amount of direct costs incurred (i.e., no rate of return or cost of money) should be recovered in rates by some method determined in a rate case, as long as such an allowance is not somehow improper (e.g., retroactive rate making, contrary to some mandatory accounting/rate making principle, etc.).

8. Within 5 years of obtaining approval for cost recovery of the CAP costs, the water company must submit a detailed engineering plan outlining how the water will be put to use.

9. If a water company that has obtained cost recovery from the Commission is not using its total CAP allotment by 2034, that portion not being used shall be sold. If a water company has recovered from ratepayers the cost for retaining that portion of the CAP allocation it sells, all net proceeds shall be refunded to ratepayers in a manner to be determined by the Commission at that time. Similarly, if a water company sells all or any portion of its CAP allocation after recovering from ratepayers the cost to retain the portion it sells, all net proceeds shall be refunded to ratepayers.

STAFF'S RESPONSES TO ARIZONA WATER COMPANY'S FIFTH SET OF DATA REQUESTS ACC DOCKET NO. W-01445A-02-0619

July 28, 2003

5.1 On page 10 of the Direct Testimony of Lyndon R. Hammon at line 23, it states that Staff's difference from the Company's *pro forma* expense is mainly due to ADEQ rule changes for the inclusion of radio-chemicals in the MAP program.

(a) What is ADEQ's requirement, if any, for testing for radio-chemicals on new wells?

(b) Are these tests included in the MAP tests?

(c) If not, has staff allowed testing costs for these required tests?

Response: See attached

(a) The ADEQ requirements are delineated in the Arizona Administrative Code, R-18-4-505.B.1., "Approval To Construct", which states:
"1. An application for Approval to Construct, including the following documents and data, shall be submitted to the Department:
(a) Detailed construction plans…
(b) Complete specifications…
(c) A design report…
(d) **Analyses of a proposed new source of water…**"

Sometimes this information is not available during the design stage (e.g., the well may be drilled but not equipped), and DEQ will make its construction approval conditional upon acceptable biological and chemical analyses. The "Approval Of Construction" (operational approval) will be given co-incident with DEQ's receipt of those analyses and inspection results.

(b) No. Initial testing is not performed by MAP and the initial testing cost is the responsibility of the water company. Subsequent testing is performed by MAP, if the water company qualifies by size.

(c) No. Staff would not normally recommend the inclusion of future prospective costs as an annual, recurring expense. This initial testing is a one time, non-recurring cost. Instead, Staff would recommend that this type of cost be capitalized and included in the development costs of the well, as construction plans, engineering specifications, and design reports, should be similarly treated.

Response by: Lyndon Hammon

STAFF'S RESPONSES TO ARIZONA WATER COMPANY'S SIXTH SET OF DATA REQUESTS ACC DOCKET NO. W-01445A-02-0619

July 31, 2003

6.1 On page 10 of the Direct Testimony of Ronald E. Ludders at line 18, Mr. Ludders testifies in reference to purchased power adjustor mechanisms that "[c]urrently, Arizona Water Company is the only water provider still using this adjustor."

a) Please identify all water companies that have had adjustor mechanisms in the past ten years.
b) In reference to a) above, provide the date or timeframe when the adjustor mechanisms were eliminated and a reference to the Commission Decision.
c) Please provide the names of any utilities regulated by the Arizona Corporation Commission that currently have purchased power adjustment mechanisms.
d) In reference to the response to c) above, has the Commission Staff made any recommendations in Staff reports or testimony to eliminate the purchased power adjustment mechanisms of any of the identified entities in the past five years?
e) If the answer to d) above is affirmative, please provide list of Company names, docket numbers and Commission decisions.

Response: Pursuant to Rule 33(c), Ariz.R.Civ.Pro., please be advised that the information sought is located in the most recent rate decisions for each company and in the current tariffs of each company. The most recent rate decisions are located in the Commission's docket control center, located at 1200 West Washington, Phoenix. The current tariffs are on file with the Commission's Tariff Administrator, who is located at the same address.

Response by: Claudio Fernandez for Ronald E. Ludders

Sheryl Hubbard

From: JSHAPIRO@FCLAW.COM
Sent: Friday, August 01, 2003 11:04 AM
To: Ralph Kennedy; RJKenndy@extremezone.com; Bob Geake; Sheryl Hubbard; Bill Garfield
Subject: FW: Arizona Water's 6th Set of Data Requests

FYI.

-----Original Message-----
From: Tim Sabo [mailto:TSabo@admin.cc.state.az.us]
Sent: Friday, August 01, 2003 10:54 AM
To: SHAPIRO, JAY
Subject: RE: Arizona Water's 6th Set of Data Requests

Regarding 6.1, the only one we are aware of is Bella Vista. Bella Vista had a Purchased Power Adjustor, which was eliminated in Decision 61730 (Jun 4, 1999). Regarding 6.2, the reclassification adjustment was done because the item was inventory, but was listed as an expense. I don't know if it was chemicals, or filters or what. Ron will be back on Monday, and if the Company needs the details, Mr. Kennedy or Ms. Hubbard can give him a call. The other part of the adjustment was to use actual 2002 expenses, rather than "pro forma" 2002 expenses.

>>> <JSHAPIRO@FCLAW.COM> 07/31/03 04:18PM >>>
Tim--we have reviewed the responses that were just provided to Arizona Water's 6th set of data requests and have two areas of concern.

First, with respect to 6.1, although the Company really should not be expected to gather the orders themselves given that Staff has repeatedly insisted that this and other utilities obtain publicly available information for Staff in response to data requests, at a minimum Staff must identity the names of the water companies requested in subsection (a).

Second, Staff's response to 6.2 seems to explain what the adjustment is, but not the basis, which is the focus of the question. Therefore, the answer is non responsive.

We would like revised answers by 2:00 p.m. Friday, August 1, 2003 in light of our rapidly approaching rebuttal deadline. Please let me know immediately if Staff will not provide these additional responses.

Jay

-----Original Message-----
From: Tim Sabo [mailto:TSabo@admin.cc.state.az.us]
Sent: Thursday, July 31, 2003 3:27 PM
To: SHAPIRO, JAY; JAMES, NORM
Subject: Arizona Water's 6th Set of Data Requests

Attached is Staff's response to Arizona Water's 6th Set of Data Requests.

Let me know if you have any questions.

The information contained in this message may be protected by the attorney-client privilege. Please immediately reply to the sender of this e-mail if you have received it in error, then delete it. Thank you.

For more information on Fennemore Craig, please visit us at http://www.fennemorecraig.com.